BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal)
of)
HUNTINGTON PARK FIRST SAVINGS AND)
LOAN ASSOCIATION)

Appearances:

For Appellant: Philip C. Jones, Attorney at Law

For Respondent: Paul L. Ross, Associate Tax Counsel

O P I N I O N

This appeal is made pursuant to Section 26077 of the Revenue and Taxation Code from the action of the Franchise Tax Board in denying the claims of Huntington Park First Savings and Loan Association for refund of franchise tax in the amounts of $658.35, $1,090.82, $1,413.74 and $1,628.54 for the income years 1948, 1949, 1950 and 1951, respectively.

Appellant commenced business in California as a federal savings and loan association in 1936. Prior to 1943 the Franchise Tax Commissioner (predecessor of the Franchise Tax Board) had not allowed savings and loan associations to deduct from their income additions to a reserve for bad debts. In a prolonged effort to obtain the right to such deductions representatives of the California Savings and Loan League held a series of conferences with the Commissioner. This league was composed of associations such as, and included, the Appellant. In 1943, as the result of the conferences, the then counsel for the Commissioner sent a letter to the executive vice-president of the league, setting forth the agreement which was reached. Pertinent excerpts from the letter are as follows:

* * *

"We have now concluded, after making a study of the bad debt experience of building and loan, and savings and loan institutions in this State, to allow your members to claim a deduction for a reasonable addition to a reserve for bad debts. However, the right to this deduction will be subject to the following qualifications+

"(1) An association may claim an amount equivalent to ,002 of its outstanding loan accounts at the beginning of any particular income-j%& as a reasonable addition to a reserve for bad debts,

"(2) Associations desiring to follow this method must set up an account denoted as a reserve for bad debts. This account will be in addition to the insurance and loss accounts maintained by these associations in pursuance to Federal regulations.

"(3) Associations desiring to take advantage of this method must file with the Commissioner, within the immediate future, a statement which will set forth that they have elected to use the 'reserve method' for future years, together with a statement showing whether they have used the 'reserve method' or the 'actual bad debt method' on returns filed within the last four years."

* * *

"(6) The *reserve method' set forth herein must be used by associations for all years open under our statute of limitations provided the associations have been using the 'reserve method' exclusively during that period of time or provided the associations have not used either method during that period of time.

"(7) Those associations electing to take advantage of the 'reserve method' may claim a deduction for such reserve in their returns which they will file in the near future for the 1943 taxable year."

Appellant did not learn of this letter until 1953, when it filed amended returns for the years in question, 1949 through 1951, claiming deductions for additions of .002 of its outstanding loans for those years to a bad debt reserve, and filed claims for refund. It had not claimed any manner of deduction for bad debts in those years; it did not suffer any actual bad debts in those years; and it did not maintain bad debt reserve accounts on its books during those years. The Franchise Tax Board denied the claims for refund,

Several aspects of this matter have been thoroughly argued by the parties. However, we believe the following points are conclusive, It is apparent from the letter (paragraph 3) that to take advantage of its provisions for retroactive claims the election was to have been made "in the immediate future." It is clear that the year 1953 is not "in the immediate future" from

1943. Whether or not the allowance by the Commissioner of the deduction in 1943 for past years was proper, at this late date the letter does not constitute an approval by the Franchise Tax Board of the use by Appellant of the reserve method of treating bad debts for the years in question, and it cannot now be used as authority for claiming deductions retroactively for those years. The allowance of the claims for refund, accordingly, depend upon the applicable provisions of the law and regulations.

Section 24121f of the Revenue and Taxation Code provides for deduction of "Debts which become worthless within the income year; or, in the discretion of the Franchise Tax Board, a reasonable addition to a reserve for bad debts," (Underscoring added.) The regulations provide that "A taxpayer filing a first return of income may select either of the above two methods subject to approval by the Franchise Tax Board upon examination of the return. If the method selected is approved, it must be followed in returns for subsequent years, except as permission may be granted by the Franchise Tax Board to change to another method. Application for permission to change the method of treating bad debts shall be made at least 30 days prior to the close of the income year for which the change is to be effective," and that "Taxpayers who have established the reserve method of treating bad debts and maintained proper reserve accounts for bad debts may deduct from gross income a reasonable addition to a reserve for bad debts in lieu of a deduction for specific bad debt items" (Title 18, California Administrative Code, Section 24121f(1)-24121f(4).

There is no reason to believe the regulation exceeds the authority of the Franchise Tax Board, nor has the Appellant so claimed, Appellant had not established the reserve method nor maintained a reserve account during the years for which it claims refunds. In addition, the federal cases establish that an addition to a reserve for bad debts cannot be made after the close of the year (Farmville Oil & Fertilizer Co, v. Commissioner, 78 Fed, 2d 83; Hogan v. Commercial Discount Co., 149 Fed. 2d 585, cert. den. 326 U.S. 764.) Appellant has pointed to no authority to the contrary. We conclude that the Franchise Tax Board must be sustained,

O R D E R

Pursuant to the views expressed in the opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 26077 of the Revenue and Taxation Code, that the action of the Franchise Tax Board in denying the claims of Huntington

Appeal of Huntington Park Savings and Loan Association

Park First Savings and Loan Association for refund of franchise tax in the amounts of $658.35, $1,090.82, $1,413.74 and $1,628.54 for the income years 1948, 1949, 1950 and 1951, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this 1st day of November, 1955, by the State Board of Equalization.

J. H. Quinn, Chairman

Paul R. Leake, Member

Robert E. McDavid, Member

Geo. R. Reilly, Member

Robert C. Kirkwood, Member

ATTEST: Dixwell L. Pierce, Secretary